

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 00-25**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Application of Tennessee sales and use tax to charges for transporting natural gas.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] is a division of [CITY IN TENNESSEE], created by an [ACT] which authorized the taxpayer to construct, purchase, operate and maintain a gas plant and/or system. Pursuant to its authority to operate a gas system, the taxpayer engages in a number of discrete activities relating to the purchase, sale and transportation of natural gas. For the purpose of this ruling request, the taxpayer engages in the following two separate activities.

First, the taxpayer purchases natural gas from [COMPANY] or others on the spot market. The taxpayer accepts delivery or title to such gas at a point where the taxpayer's transmission system connects with [COMPANY]'s transmission system. From this point of delivery, the taxpayer assumes ownership of the gas ("Taxpayer Owned Gas"). The taxpayer sells its purchased gas to its customers in Tennessee and collects sales tax on all such sales, including tax on charges for transporting the gas. Commercial customers purchase the taxpayer's gas under a number of contractual arrangements. Under the sample contract provided with the ruling request, the taxpayer agrees to sell and deliver natural gas to the customer. The point of delivery of the gas is the point where the taxpayer's service pipe crosses the boundary of the customer's property. Title to and possession of the gas passes to the customer at that point.

Second, companies within the taxpayer's service area (generally [COUNTY], Tennessee) may make arrangements to purchase their own gas in the spot market or directly from [COMPANY] ("Privately Owned Gas"). The taxpayer is the only company granted a franchise to operate a gas system in [COUNTY], Tennessee. Thus, private companies acquiring gas on their own enter into a Gas Transportation Service Agreement (the "Agreement")¹ pursuant to which the taxpayer agrees to transport the Privately Owned Gas over the taxpayer's gas system from the [COMPANY] pipeline to the private company. Pursuant to the agreement, the point of delivery of the Privately Owned Gas is the point where the taxpayer's service pipe crosses the boundary of the private company's property. The private company is charged for the transportation of Privately Owned Gas.

A customer that purchases gas transportation services may sometimes also purchase Taxpayer Owned Gas under the Agreement when the customer cannot acquire gas from [COMPANY] or on the spot market. In such an instance, the taxpayer bills separately for Taxpayer Owned Gas sold to the customer and for transportation charges for Privately Owned Gas.

QUESTIONS

1. Are transportation charges for Taxpayer Owned Gas, which are charged in connection with the sale of Taxpayer Owned Gas, subject to Tennessee sales tax?
2. Are transportation charges for Privately Owned Gas acquired by private companies or entities at the point of origin and transported by the taxpayer to the private company at the boundary of the private company's property subject to Tennessee sales tax?

¹A copy of the agreement was provided with the ruling request.

3. Can the taxpayer give a credit to any private entity that has erroneously paid to the taxpayer sales tax on transportation charges for Privately Owned Gas?
4. If the taxpayer has erroneously paid sales tax to the Department of Revenue ("the Department") with respect to transportation charges for Privately Owned Gas, is the taxpayer required to file a claim for refund with the Department in order to receive a refund or credit for such erroneous payments, or may the taxpayer take a corresponding credit on its sales and use tax returns for credit allowed to its customers for such erroneous sales tax payments?
5. If sales tax has been erroneously paid to the Department, what is the statute of limitations on requesting a refund or credit for such erroneous payments?

RULINGS

1. Yes.
2. No.
3. Yes.
4. The taxpayer must file a claim for refund with the Department in order to receive a refund or credit for erroneously paid sales or use tax. The taxpayer cannot take a credit on a current sales and use tax return for prior overpayments without first filing a claim for refund with the Department and having the Department grant the taxpayer a credit.
5. In order to receive a refund or credit for erroneously paid sales or use taxes, the taxpayer must file a claim for refund with the Department, under oath and supported by proper proof, within three years from December 31st of the year in which the payments were made.

ANALYSIS

1. Under the first transaction described in the facts, the taxpayer purchases natural gas from a supplier, taking title to and possession of the gas (referred to in the facts as "Taxpayer Owned Gas"). The taxpayer subsequently sells this gas to its customers in Tennessee and collects Tennessee sales tax on all such sales. As part of the transaction, the taxpayer agrees to deliver the gas to the customer. The point of delivery is the point where the taxpayer's service pipe crosses the boundary of the customer's property. The question presented is whether charges for transporting the gas sold to customers is subject to sales tax as part of the sale of Taxpayer Owned Gas.

Natural gas is tangible personal property. See T.C.A. § 67-6-102(29). The sale of

tangible personal property in Tennessee is subject to tax under the Retailers' Sales Tax Act. T.C.A. § 67-6-202. The tax base is the "sales price" of the tangible personal property, defined in pertinent part as:

"the total amount for which...tangible personal property is sold, including any services that are a part of the sale of tangible personal property...."

T.C.A. § 67-6-102(26).

Accordingly, the charge for transporting Taxpayer Owned Gas is subject to sales tax if it constitutes a service that is part of the sale of the gas. The following rule governs when a transportation charge is part of the sales price:

Freight, delivery, or other like transportation charges are subject to the Sales and Use Tax if title to the property being transported passes to the vendee at the destination point. Where title to the property being transported passes to the vendee at the point of origin, the freight or other transportation charges are not subject to the Sales or Use Tax. It is immaterial whether the vendor or vendee actually pays for any charges made for transportation, whether the charges are actually paid by one for the other, or whether a credit or allowance is made or given for such charges. In cases where a vendor makes a separate charge for delivering tangible personal property in his own vehicle, or makes arrangements for delivering tangible personal property, other than by a common carrier, the delivery charges shall be considered a part of the selling price subject to the Sales or Use Tax.

Tenn. Comp. R. & Regs. 1320-5-1-.71.

Under the facts at issue, title to and possession of the gas pass to the customer at the customer's property, the destination point. Accordingly, the transportation charges are part of the sales price and are subject to sales tax.

2. In contrast to the Taxpayer Owned Gas, the taxpayer does not purchase or sell the Privately Owned Gas. Instead, the Privately Owned Gas is sold directly from [COMPANY] or some other supplier to the ultimate consumer. The taxpayer only provides a transportation service. Accordingly, the transportation service is not performed as part of the sale of tangible personal property in the second transaction described in the facts. *See Austin Co. v. Woods*, 620 S.W.2d 73 (Tenn. 1981)(holding that services provided by a third party to the sale are not part of the sale of tangible personal property under the definition of "sales price").

Certain enumerated services are subject to sales tax independently of any sale of tangible personal property. See, e.g., T.C.A. § 67-6-102(24)(F). Transportation services,

however, are not among the specifically taxable services.

Consequently, charges for transporting Privately Owned Gas are not subject to sales tax under the facts provided.

3. If a customer has erroneously paid sales tax to the taxpayer with respect to non-taxable transportation services, the taxpayer can allow that customer a credit for the erroneously paid tax. Furthermore, granting the customer a credit or a refund of such tax must be done before the taxpayer can receive a credit or refund of the tax from the Department. T.C.A. § 67-1-1802(a); Tenn. Comp. R. & Regs. 1320-5-1-.79.

4. The taxpayer cannot, however, unilaterally take a credit on a current sales and use tax return for taxes that were erroneously paid in a prior period. T.C.A. § 67-1-1802 provides the remedy in cases where taxes have been paid in error. That section contains certain requirements that must be satisfied, including, in most cases, the requirement that a timely claim be filed with the Department. While T.C.A. § 67-1-1802 provides certain limited exceptions to this requirement, none of those exceptions apply under the facts presented.

Allowing a credit for prior erroneous payments against current or future tax liabilities is synonymous with granting a refund under T.C.A. § 67-1-1802. In the case of a refund, the taxpayer would tender the amount due for the current month and receive funds back for the prior erroneous payment. In the case of a credit, the taxpayer would simply tender the net amount. There is no relevant distinction between the two. Thus, no such credit can be allowed unless the requirements set out in T.C.A. § 67-1-1802 are met. This conclusion is further supported by administrative rule. Tenn. Comp. R. & Regs. 1320-5-1-.79 states that “[n]o credit for overpayment of taxes may be given unless a person claiming credit would have a right to receive the credit by means of a Claim for Refund.”

Consequently, the taxpayer cannot take a credit for prior erroneous payments without filing a formal request with the Department of Revenue.²

5. With respect to the statute of limitations for filing a claim for refund, the applicable statute states in pertinent part as follows:

The authority [of the commissioner of revenue to grant a refund] extends only to taxes for which a claim is filed, with the commissioner under oath and supported by proper proof, within three (3) years from December 31 of the year in which the payment was made.

² It should be noted that certain statutory provisions specifically allow credits without filing a claim for refund. *See, e.g.*, T.C.A. §67-6-346 (allowing a purchaser to take credit for sales and use tax paid with respect to pollution control). The facts provided here do not involve the application of any specific statutory credits, and this ruling does not address such provisions.

T.C.A. § 67-1-1802(a)(1).³

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APPROVED: Ruth E. Johnson
Commissioner

DATE: 8-11-00

³Tenn. Comp. R. & Regs. 1320-5-1-.79 currently states that a claim for refund must be filed within the time period provided by T.C.A. § 67-1-707 (one year). However, that rule was last amended in 1983 and has been superceded by T.C.A. § 67-1-1802(a), which was enacted in 1986. Chapter 749 of the Public Acts of 1986.